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United States Bankruptcy Court
San Jose, California

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re] Case No. 04-53596-ASW
]
DYMOND CONSTRUCTION GROUP, INC.,] Chapter 11
]
Debtor.]

MEMORANDUM DECISION
DENYING CREDITOR'S MOTION FOR ALLOWANCE
AND PAYMENT OF ADMINISTRATIVE CLAIM

Before the Court, in the above-captioned chapter 11¹ case, is
Carpenter Funds Administrative Office of Northern California's
("Creditor")² *Motion For Allowance and Payment of Administrative*

¹ Unless otherwise noted, all statutory references are to
Title 11, United States Code (the Bankruptcy Code), as it existed
when Debtor filed its bankruptcy petition on June 4, 2004.

² Creditor performs administrative services for Carpenters
Health and Welfare Trust for California, Carpenters Pension Trust
Fund of Northern California, Northern California Carpenters
Vacation and Holiday Plan, Carpenters Annuity Trust Fund for
Northern California, Carpenters Contract Work Preservation Trust
Fund, Carpenters Apprenticeship and Training Trust Fund for

1 *Claim Against Debtor Dymond Construction Group, Inc. ("Debtor"),*
2 *seeking allowance and payment of administrative expenses pursuant*
3 *to 11 U.S.C. § 507(a)(1) for actual and necessary expenses of*
4 *preserving and protecting property of the estate of the debtor,*
5 *Dymond Construction Group, Inc. ("Allowance Motion"). Debtor filed*
6 *a response, opposing Creditor's Allowance Motion on the grounds*
7 *that: (1) Creditor filed duplicate claims; (2) Creditor overstated*
8 *its claims; and (3) Creditor is not entitled to an administrative*
9 *claim ("Opposition").*

10 This matter was briefed and argued and the parties submitted
11 post-hearing briefs. Debtor is represented by Sean M. Jacobson,
12 Esq. of the Law Offices of Cohen and Jacobson; Creditor was
13 previously represented by David A. Bohl, Esq. of Weinberg, Roger
14 and Rosenfeld, a Professional Corporation, and is now represented
15 by Christian L. Raisner, Esq. and Alan G. Crowley, Esq. of
16 Weinberg, Roger & Rosenfeld, a Professional Corporation. The
17 Official Committee of Unsecured Creditors ("Creditors' Committee")
18 is represented by Charles E. Logan, Esq. of the Law Offices of
19 Charles E. Logan. Secured creditor Steve Williams ("Williams") is
20 represented by Kathryn S. Diemer, Esq. of Diemer & Whitman, LLP.

21 After oral argument, the Court requested that the parties
22 submit post-hearing briefs addressing the issue of whether, under
23 the specific facts presented here, a pre-petition priority claim

24 _____
25 Northern California and the Carpenters Industry Advancement Trust
26 Fund (collectively, "Carpenter Funds"). The Carpenter Funds are
27 all employee benefit plans established by collective bargaining and
28 trust agreements and are governed by the Employee Retirement Income
Security Act of 1974 ("ERISA") § 3(3). Hereinafter, since
"Creditor" filed the pleadings on behalf of the "Carpenter Funds,"
references to "Creditor" includes the "Carpenter Funds."

1 can be transformed into an administrative claim when the contract,
2 which forms the basis for the claim, was not assumed. The Court
3 identified relevant case law for the parties to address in their
4 briefs.

5 At the time this matter was submitted the only disputed issue
6 remaining for this Court to decide was whether Creditor was
7 entitled to an administrative claim or a pre-petition priority
8 claim. The parties stipulated at the January 20, 2006, hearing
9 that the amount of Creditor's claim, whether determined to be a
10 priority claim or an administrative claim, was \$58,251.40.³

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13 ³ Creditor filed two proofs of claim in Debtor's bankruptcy
14 case. On July 28, 2004, Creditor filed a claim in the amount of
15 \$203,843.07 ("First Claim"). The First Claim states that it is a
16 priority claim under §§ 507(a)(3) and (a)(4) in the amount of
17 \$185,311.88 and an unsecured claim in the amount of \$18,531.19. Of
18 the \$185,311.88 priority amount, the claim indicates that
19 \$30,427.10 represents a claim under 11 U.S.C. § 507(a)(3) and
20 \$154,884.78 under § 507(a)(4). On September 28, 2004, Creditor
21 filed a second priority claim in the amount of \$149,284.75 ("Second
22 Claim").

23 After credit was given for payments made by the Debtor, the
24 parties resolved the issues regarding the amount of Creditor's
25 claim and stipulated at the hearing that the actual amount of the
26 claim is \$58,251.40. Creditor retreated from this position
27 somewhat in its post-hearing brief, stating that:

28 while the Carpenters Trust Funds agreed that if their
claim was determined to be a 507(a)(4) priority claim,
then, and only then, would they agree that such a pre-
petition priority claim would be for \$58,251.40.

However, if the Court determines that the Carpenters
Trust Funds' claim should be allowed as an Administrative
Claim, then the Carpenters Funds' claim of unpaid
contributions, for which new consideration was given, is
for \$98,359.93 plus the attorneys' fees incurred in
arguing this Motion before the Court.

Creditor's post-hearing brief at 6:17-22. Because the Court finds
that Creditor's claim is entitled to priority, rather than
administrative status, the amount of the claim remains undisputed
at \$58,251.40.

1 This Memorandum Decision constitutes the Court's findings of
2 fact and conclusions of law, pursuant to Rule 7052 of the Federal
3 Rules of Bankruptcy Procedure.

4
5 I.

6 STATEMENT OF FACTS

7 On June 4, 2004, Debtor filed a voluntary petition under
8 chapter 11 of the Bankruptcy Code.

9 Debtor is engaged in the construction business, and employs
10 carpenters on construction jobs. Prior to filing its petition,
11 Debtor entered into a collective bargaining agreement ("CBA") with
12 Carpenters 46 Northern California Counties ("Union") under which
13 the Union agreed to provide Debtor with carpenters to work on
14 Debtor's construction projects. Debtor paid the Union certain dues
15 and benefits in exchange for the Union providing health care
16 insurance and benefits to Debtor's carpenters.⁴

17 On July 28, 2004, Debtor filed a motion to assume the CBA
18 ("Assumption Motion"). In the Assumption Motion, Debtor explained
19 that it had failed to pay pre-petition dues and benefits called for
20 by the CBA for the months of February, March, April and May of
21 2004, resulting in the Union's suspension of the health care
22 benefits of Debtor's employees. Debtor sought to assume the CBA

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27 ⁴The Union provides these benefits to Debtor's employees
28 through Creditor, its servicing agent. Debtor makes payments
pursuant to the CBA directly to Creditor. Creditor filed the claim
at issue in this case.

1 because, Debtor contended, the contract was critical to its
2 continued operations.⁵

3 Debtor's Assumption Motion was opposed by both Williams and the
4 Creditors' Committee, and a hearing on the Assumption Motion
5 occurred on August 2, 2004. Williams opposed the motion
6 specifically to prevent the creation of an administrative claim for
7 Creditor.⁶ At the hearing, Debtor, Creditor, Williams and the
8 Creditors' Committee entered into an interim agreement whereby the
9 Debtor agreed to remain current on the post-petition union dues⁷
10 payments and make one additional monthly payment to be applied to
11 the February 2004 delinquency, and the hearing on the Assumption
12 Motion was continued to September 2, 2006. The Court instructed
13 the parties to attempt to reach a mutually agreeable resolution
14 prior to the continued hearing.

15 At the September 2, 2004, hearing, Debtor, Creditor, Williams
16 and the Creditors' Committee announced that they wished to enter
17 into a stipulation to resolve the Assumption Motion
18 ("Stipulation"). At the hearing, Debtor stated that the payments

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20 ⁵ See July 28, 2004, Declaration of Kent Caskey in support of
21 the Assumption Motion ("Caskey Declaration") at 2:18-21.

22 ⁶ See February 3, 2006, Declaration of Kathryn Diemer in
23 support of Debtor's Opposition ("Diemer Declaration"), ¶ 2, and the
24 February 3, 2006, Declaration of Lawrence A. Jacobson in support of
25 Debtor's Opposition, ¶ 2.

26 ⁷ The parties, both in their papers and at the hearings on
27 this matter, used the terms "union dues" and "fund contributions"
28 interchangeably. It appears to the Court that the proper term for
the payments at issue is "fund contributions." However, because
the language of the Stipulation and Order refers to "union dues,"
for the sake of consistency, this decision will refer to the
payments owed by Debtor to Creditor pursuant to the CBA as "union
dues."

1 pursuant to the Stipulation were to be applied toward Creditor's
2 claim as filed and as scheduled by the Debtor as a priority claim
3 under § 507(a)(3) and (4). Mr. Bohl, counsel for Creditor,
4 specifically assented to such treatment of Creditor's claim.³ At
5 the hearing, Counsel for Williams articulated on the record that
6 the negotiations leading to the Stipulation (involving herself,
7 counsel for Debtor, Creditor and the Creditors' Committee)
8 specifically did not contemplate assumption of the CBA. In fact,
9 according to the declaration of Williams' counsel, this was the key
10 point in the negotiations, and neither Williams nor the Creditors'
11 Committee would have agreed to any resolution that gave Creditor an
12 administrative claim.⁹ The consent of secured creditor Williams
13 was required because the Debtor used Williams' cash collateral to
14 pay Creditor pursuant to the Stipulation.¹⁰ The parties, including
15 counsel for Creditor, signed off on the Stipulation.

16 On or about September 3, 2004, this Court entered an order
17 approving the Stipulation ("Order"), pursuant to which the
18 Assumption Motion was resolved as follows:

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21 ⁸ See Exhibit "E" to the November 1, 2005, declaration of Alan
22 Crowley in support of Creditor's Allowance Motion ("Crowley
23 Declaration"), which is a copy of the transcript from the
September 2, 2004, hearing ("September 2, 2004, Transcript") at
4:11-23.

24 ⁹ See September 2, 2004, Transcript at 6:16-25. See also
Diemer Declaration at 2:19-25.

25 ¹⁰ Williams agreed only to the use of his cash collateral for
26 the purpose of making payment for the first month of delinquent
27 pre-petition union dues. The parties understood that any other
28 payment toward the delinquency would be made out of profits.
Diemer Declaration at 2:10-12.

(1) the [CBA] will **not** be assumed at this time as requested by the [Assumption Motion]; (2) Debtor will stay current on payment of the union dues; (3) Debtor **is permitted** to cure the pre-petition arrearages in the union dues over a period of three months, with one delinquent payment to be made each month along with the current dues; and (4) that benefits will be restored on an ongoing basis, with full restoration of all benefits to occur upon receipt of the final cure payment.

Order at 2:2-7 (emphasis added). Debtor remained current on payment of the post-petition union dues. However, Debtor was unable to make all of the permitted payments on the pre-petition arrearage.

Although the terms of the Stipulation and Order stated that health benefits for the pre-petition period would be restored only upon Debtor making the final cure payment, Creditor in fact, because of its own internal mistake, granted credit to Debtor's employees in September 2004, for health care coverage for the pre-petition months of March, April, May and June 2004, for which Creditor had not received full payment. Creditor estimated that Debtor's carpenters submitted claims for benefits totaling \$18,051.00 for May and \$15,539.00 for June.¹¹ Creditor did not supply any figures for the months of March and April.

Creditor's Allowance Motion stated that Creditor gave credit to Debtor's employees for health care benefits because of Debtor's repeated representations that it would make double payments¹² to

¹¹ See Crowley Declaration, ¶ 12. In support of these estimates, Creditor attached an untitled spreadsheet to the Crowley Declaration as Exhibit 'G' stating the figures for the estimated benefits provided to Debtor's employees.

¹² For example, when the August 2004 payment was due, Debtor would pay Creditor the equivalent of two monthly dues payments -- one for the current month (August) and one to be applied to the delinquent monthly payments (March 2004).

1 cure the arrearage.¹³ However, this was directly contradicted by
2 the statement of Creditor's counsel during the January 20, 2006,
3 hearing, when he explained that the credit was given due to an
4 internal error on the part of Creditor.¹⁴ Creditor's Allowance
5 Motion argued that the credited health coverage caused Debtor's
6 employees to continue working for Debtor, which enabled Debtor to
7 remain in business.¹⁵

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9 ¹³ See Crowley Declaration, ¶ 10. As evidence of Debtor's
10 representations that it would cure, Creditor cites to a letter from
11 Debtor's counsel to the parties dated August 17, 2004 ("Letter").
12 The Letter is attached to the Crowley Declaration as Exhibit 'D'.
13 In the Letter, Debtor's counsel stated: "Debtor will stay current
14 with the dues and cure the arrearages over the next three months,
15 with the union releasing the hour banks upon payment of the
16 delinquent months."

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18 ¹⁴ At the January 20, 2006, hearing, the following conversation
19 occurred between the Court and Creditor's Counsel Alan Crowley:

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21 Crowley: The Trust Funds released the banked hours, which allowed
22 the Debtor's employees to have health care benefits. If
23 they had only released one month of hours, then Debtor
24 would have been back here before the court, asking you
25 for more cash collateral or asking for the exact same
26 motion to reoccur. So it was only because the Trust
27 Funds released four months of banked hours for health
28 care coverage that enabled their employees to continue to
get health care coverage, to keep their employees around,
to keep in business. Only because of that was the Debtor
kept from coming back to strike the same deal for the
next month, or from paying over the next few months. So
that's a little bit different than these cases, which I
haven't briefed, and I understand there's a difference...

Court: Have you read them?

Crowley: Admittedly no. But that's the difference here. They got
the benefit of four months of health care coverage...

Court: But why did you do that?

Crowley: That was an error on the part of the Trust Funds with
respect to the way their computer system credits hours to
employees.

¹⁵ Debtor admitted before entering into the Stipulation that
some agreement with the Union concerning payment for employee

1 Debtor asserted that, in addition to the clear language of the
2 Stipulation and Order, Creditor consistently maintained that it
3 would not release the pre-petition benefits until Debtor cured the
4 entire delinquency.¹⁶ Debtor explained that (1) it did not know
5 that Creditor had credited any employees for health care benefits
6 until Creditor filed the Allowance Motion,¹⁷ (2) Debtor drafted its
7 disclosure statement to explain that the pre-petition health care
8 benefits would be released upon payment of Creditor's priority

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11 benefits was necessary for Debtor to remain in business. The
12 Debtor stated that:

13 The union has suspended the health care benefits of the
14 union carpenters working for Debtor because the dues have
15 not been paid. Two carpenters left employment with
16 Debtor on June 26, 2004, due primarily to the suspension
17 of the health benefits, and one more has given notice of
18 his intent to terminate his employment. Additionally,
19 Debtor is unable to employ other or replacement
20 carpenters through the union hall assignment system
21 because the union will not send those workers until
22 arrangements are made for cure of the arrearages. Due to
23 the fact that Debtor is engaged in the construction
24 industry, the continued employment of carpenter employees
25 that are represented by the union is critical to the
26 continued operation of Debtor's business.

27 Caskey Declaration, ¶¶ 4-5 (emphasis added).

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16 According to Debtor: "During the negotiations, Mr. Bohl, counsel for [Creditor], made it very clear that no back benefits would be restored until payment was received on priority portions of the arrears." February 3, 2006, Declaration of Lawrence Jacobson, ¶ 4.

17 The period of time between Creditor's crediting of the health benefits for the pre-petition period and the filing of the Allowance Motion, during which Debtor was unaware of the credit, was more than a year. Creditor granted the credit sometime in September 2004. The Allowance Motion was filed on November 11, 2005.

1 claim,¹⁸ and (3) Debtor paid in full for all post-petition benefits
2 it received from Creditor.¹⁹ Creditor does not challenge these
3 factual assertions.

4 Creditor now seeks allowance of an administrative claim for
5 delinquent pre-petition union dues.²⁰ Debtor objects to Creditor's
6 claim. While conceding that Creditor has a valid claim for the
7 unpaid, pre-petition union dues, Debtor contends that the full
8 claim should be treated as an unsecured priority claim pursuant to
9 §507(a)(3) and (4).

10 Debtor's chapter 11 plan ("Plan") was confirmed on February 1,
11 2006. The Plan did not provide for assumption of the CBA.
12 Creditor did not object to confirmation of the Plan.

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16 ¹⁸ Debtor's counsel stated: "Indeed, Dymond was not aware that
17 those benefits were released until review of the Motion, and
18 accordingly had drafted its Disclosure Statement to include that
19 those back benefits would be released upon payment of the priority
20 claim." November 21, 2005, Declaration of Lawrence Jacobson in
21 support of Debtor's Opposition, ¶ 8.

19 ¹⁹ Debtor stated that:

20 The only benefit [sic] conferred by [Creditor] during the
21 post-petition period are the benefits which have been
22 provided to the carpenters on an ongoing basis. Debtor
23 has paid the dues to [Creditor] as they have become due
24 in the post-petition period. Due to the fact that these
25 funds have been current during the post-petition period,
26 no administrative claim exists, as payment has been made
27 for any benefit.

25 November 21, 2005 Declaration of Diane McKee in support of Debtor's
26 Opposition, ¶ 6.

27 ²⁰ See n.7, supra, regarding the interchangeable use of the
28 terms "union dues" and "fund contributions."

II.

ARGUMENTS

A. Creditor's Arguments

Creditor argued that Debtor implicitly assumed the CBA by not rejecting it under 11 U.S.C. § 1113 and by continuing to make payments under the CBA. Creditor asserted that, due to Debtor's repeated insistence that it would make double payments to cure the arrears and its continued operation under the terms of the CBA, the terms of the Stipulation and Order are inconsequential in determining whether Creditor's claim is entitled to administrative status. Creditor cited In re Roth American, Inc., 975 F.2d 949 (3d Cir. 1992) and In re Adventure Resources, Inc., 137 F.3d 786 (4th Cir. 1994) in support of its assertion that a debtor can impliedly assume a collective bargaining agreement. In Roth American, the Third Circuit agreed with the union's argument that the debtor's failure to reject the collective bargaining agreement in accordance with § 1113 resulted in assumption by operation of law.²¹ 975 F.2d at 957. In Adventure Resources, the Fourth Circuit followed the decision in Roth American, holding that the collective bargaining agreement was assumed due to the debtor's failure to reject pursuant to § 1113. 137 F.3d at 798.

According to Creditor, since the CBA was assumed under its implied assumption theory, "the expenses and liabilities incurred may be treated as administrative expenses." Id. (citing NLRB v.

²¹ However, the Third Circuit immediately cautioned that "it simply does not follow, as the Union contends, that all claims under unrejected collective bargaining agreements are entitled to first priority." Roth American, 975 F.2d at 957.

1 Bildisco and Bildisco, 465 U.S. 513, 532 (1984)). Creditor argued
2 that these benefits were necessary expenses to preserve Debtor's
3 estate and therefore should be treated as administrative expenses
4 under §§ 503(b)(1)(A) and 507(a)(1). Section 507(a)(1) assigns
5 first priority to "administrative expenses allowed under section
6 503(b) of this title, and any fees and charges assessed against the
7 estate under chapter 123 of title 28." 11 U.S.C. § 507(a)(1).
8 Section 503(b)(1)(A) provides: "[a]fter notice and a hearing, there
9 shall be allowed administrative expenses, other than claims allowed
10 under section 502(f) of this title, including -- (1)(A) the actual,
11 necessary costs and expenses of preserving the estate, including
12 wages, salaries, or commissions for services rendered after the
13 commencement of the case[.]" 11 U.S.C. § 503(b)(1)(A).

14 In addition, citing the Ninth Circuit BAP decision in In re
15 World Sales, Inc., 183 B.R. 872, 877 (B.A.P. 9th Cir. 1995),
16 Creditor argued that it provided Debtor with "new consideration"
17 when it credited Debtor's employees with health benefits. The
18 debtor in World Sales was party to a collective bargaining
19 agreement that was in effect at the time it filed its chapter 11
20 petition. 183 B.R. at 873. Eighteen days after filing, the debtor
21 laid off its employees and sold its operation. Id. The debtor
22 never attempted to modify or reject its collective bargaining
23 agreement. Id. The services for which the creditor sought an
24 administrative claim related to post-petition employee benefits.
25 Id. at 874. The BAP stated that, in determining whether a claim is
26 entitled to administrative status, the court "must look not only to
27 the benefit to the estate, but also to the consideration due the
28 creditor for providing such benefit." Id. at 877. Where the

1 benefit for which payment is sought was rendered post-petition,
2 "the payment owing by the estate must be afforded administrative
3 priority." Id. Following the BAP's reasoning, Creditor contended
4 that it provided post-petition value to Debtor through the credited
5 health benefits, which constitutes "new consideration," entitling
6 its claim to administrative status under § 507(a)(1). According to
7 Creditor, the credit enabled Debtor to retain its carpenters, thus
8 providing a substantial benefit to Debtor.

9 Creditor attempted to distinguish the current matter from In re
10 Certified Air Technologies, Inc., 300 B.R. 355 (Bankr. C.D. Cal.
11 2003). In that case, the bankruptcy court held that pre-petition
12 claims for wages and benefits arising from an unrejected collective
13 bargaining agreement were not administrative expenses. 300 B.R. at
14 369. Creditor argued that the creditor in Certified Air, unlike in
15 this case, did not provide the debtor with a post-petition benefit.
16 Creditor maintained that it provided a post-petition benefit to
17 Debtor by covering Debtor's employees' pre-petition health
18 benefits, including payment of insurance claims arising during the
19 unpaid pre-petition period. Creditor asserted that the credit
20 amounted to a post-petition loan that was extended to Debtor based
21 on Debtor's representations that it would cure the pre-petition
22 arrearage. Creditor argued that the credit was an actual and
23 necessary expense of preserving and protecting the property of the
24 Debtor pursuant to § 503(b)(1)(A) because, without the credit,
25 Debtor would have lost its carpenters.

26 In a similar vein, Creditor contended that its reimbursement
27 for the credited benefits should be treated as an administrative
28 expense due to the "necessity of payment" doctrine. Generally

speaking, this doctrine may be invoked to permit payment by the debtor on pre-petition claims prior to confirmation where the payment is deemed essential to the debtor's continued operation. Nextwave Personal Comm., Inc. v. FCC, 254 F.3d 130, 136 (D.C. Cir. 2001).²² Consistent with its argument under § 503(b)(1)(A), Creditor asserts that the pre-petition health care coverage it provided to Debtor was essential to Debtor's continued operation, and should be treated as an administrative expense pursuant to the "necessity of payment" doctrine.

B. Debtor's Arguments

Debtor asserted that: (1) Creditor's mistake in releasing the benefits for the pre-petition months was not an "actual or necessary" expense to preserve and protect its property; and (2) the parties specifically agreed that the benefits that Creditor released, and with which Debtor's employees were credited, were only to be released if Debtor cured all its delinquent pre-petition payments under the CBA. The language of the Stipulation "permitted," but did not require, Debtor to cure. Debtor was, in fact, unable to do so. Debtor explained that it paid for all of the post-petition benefits it received. Debtor argued that if, as Creditor contended, the provision of benefits conferred any benefit upon Debtor, then it was an incidental benefit and "[a]n incidental benefit is not a sufficient basis to grant an administrative

²² In support of this contention, Creditor cited a number of bankruptcy court decisions outside the Ninth Circuit. See In re Equalnet Comm. Corp., 258 B.R. 368 (Bankr. S.D. Tex. 2000); In re Cajun Elec. Power Co-op., Inc., 230 B.R. 715 (Bankr. M.D. La. 1999); In re Gulf Air, Inc., 112 B.R. 152 (Bankr. W.D. La. 1989); In re Columbia Packing Co., 35 B.R. 447 (Bankr. D. Mass. 1983).

1 priority." In re D.W.G.K. Restaurants, Inc., 84 B.R. 684, 689
2 (S.D. Cal. 1988).²³ Debtor's counsel stated in his declaration that
3 the Debtor was not even aware of Creditor's mistake²⁴ (and Creditor
4 has not alleged that the Debtor was aware) and Debtor therefore
5 argued that an unnoticed mistake could not constitute a substantial
6 contribution and was in no way necessary for preserving the estate.
7 Debtor maintained that no case law exists that supports
8 transformation of Creditor's pre-petition claim into an
9 administrative claim under the facts presented here.

10 Debtor asserted that the facts of the instant case are similar
11 to the facts in Roth American, where a collective bargaining
12 agreement was neither rejected nor assumed. The Third Circuit in
13 Roth American determined that claims for wages and benefits could
14 be granted administrative status only to the extent that the wages
15 and benefits were: (1) for a period of time between the
16 commencement of the bankruptcy case and the termination of
17 employment; and (2) compensation for services rendered post-
18 petition. 975 F.2d at 957-958. Debtor asserted that the benefits
19 at issue here accrued pre-petition and therefore, under Roth
20

21
22 ²³ D.W.G.K. Restaurants involved a creditor's claim for
23 attorney's fees as an administrative expense under § 503(b)(3)(D).
24 The court refused to grant administrative status to creditor's
25 claim, holding that the services creditor's counsel provided
26 "satisfied neither the 'substantial contribution' nor the 'actual
27 and necessary' requirements of § 503(b)." 84 B.R. at 689. The
28 court commented that, "[t]he integrity of § 503(b) can only be
maintained by strictly limiting compensation to extraordinary
creditor actions which lead directly to significant and tangible
benefits to the creditors, debtor, or the estate." Id. at 690.

²⁴ See, e.g., the November 21, 2005, Declaration of Lawrence
Jacobson in support of Debtor's Opposition, ¶ 8.

1 American, Creditor's claim would only be entitled to priority
2 status and not administrative status.

3 Debtor acknowledged that the Fourth Circuit's opinion in
4 Adventure Resources is somewhat supportive of Creditor's position,
5 but distinguished that case on the facts. There, the debtor was
6 held to have assumed a collective bargaining agreement by failing
7 to modify or reject it in accordance with § 1113(f). 137 F.3d at
8 798. By assuming the collective bargaining agreement, the debtor
9 undertook an obligation to cure all existing defaults under the
10 agreement. Id. The post-petition assumption of the contract
11 effectively transformed the pre-petition claims thereunder into
12 post-petition claims entitled to administrative status. Id.
13 Debtor insists that most important factual distinction is that the
14 contract in Adventure Resources had been assumed -- something that
15 the parties in this matter specifically agreed not to do, as
16 evidenced in the Stipulation and Order. Therefore, Debtor argued
17 that Adventure Resources is inapposite to the disposition of this
18 dispute.

19 Debtor focused its analysis on Certified Air because it
20 specifically addressed the issue of the priority of a claim for
21 arrears under a collective bargaining agreement. Debtor explained
22 that the bankruptcy court in Certified Air recognized that the
23 "plain language of a statute is conclusive as to its meaning when
24 the statutory scheme is coherent and consistent." 300 B.R. at 336.
25 Furthermore, the court in Certified Air determined that since §
26 1113 is silent as to priorities, it must be inferred that Congress
27 did not intend to grant administrative priority to arrears under
28 collective bargaining agreements. Id. at 367.

Debtor argued that Creditor specifically agreed, through the Stipulation, Order and counsel's statements at hearings before the Court, that its claim would not be granted administrative status and that the CBA would not be assumed. Debtor urged the Court to consider only the Stipulation, Order and prior testimony to evaluate the priority of Creditor's claim.

III.

ANALYSIS

The party seeking allowance of an administrative claim has the burden of proving that its claim is entitled to administrative priority. D.W.G.K. Restaurants, 84 B.R. at 689. "[S]ince an administrative expense constitutes a priority claim, any recovery must be subject to strict scrutiny by the court," and therefore the party seeking administrative priority "bears a heavy burden." Id. Limiting administrative priority, "keep[s] fees and administrative expenses at a minimum so as to preserve the estate for the benefit of all creditors." In re Sedona Institute, 220 B.R. 74, 79 (B.A.P. 9th Cir. 1998).

A. Creditor's Implied Assumption Argument

The parties agree that the CBA was valid and enforceable at the time of the bankruptcy filing. Section 1113 sets forth the procedure for the rejection of collective bargaining agreements. Section 1113(f) provides that "[n]o provision of this title shall be construed to permit a trustee to unilaterally terminate or alter any provisions of a collective bargaining agreement prior to compliance with the provisions of this section." 11 U.S.C. § 1113(f). Creditor argued that because Debtor did not reject the

1 CBA pursuant to the requirements of § 1113, Debtor impliedly
2 assumed it and therefore the pre-petition arrears were transformed
3 into an administrative expense.

4 It is true that, under certain circumstances, a collective
5 bargaining agreement may be assumed as a result of the debtor's
6 failure to reject the agreement in accordance with § 1113. Section
7 1113 "plainly imposes a legal duty on the debtor to honor the terms
8 of a collective bargaining agreement, at least until that agreement
9 is properly rejected." Adventure Resources, 137 F.3d at 796. It
10 is likewise true that the assumption of a collective bargaining
11 agreement, either express or implied, may convert a pre-petition
12 claim into an administrative expense. Id. at 798. However, while
13 § 1113 clearly prohibits unilateral modification of a collective
14 bargaining agreement, it encourages mutually satisfactory
15 modification.²⁵ In fact, consensual modification of the agreement
16 must be attempted before it may be rejected. 11 U.S.C. §
17 1113(b)(1). Based on the specific language of the Stipulation and
18 Order, the CBA was neither assumed nor rejected, but was
19 effectively modified with the consent of the parties. The Court is
20 convinced by these documents, combined with the declarations of
21 record and arguments of counsel, that the CBA was not implicitly
22 assumed, but rather was explicitly not assumed.

23
24 ²⁵ See Adventure Resources, 137 F.3d at 796, n.13 ("If the
25 debtor believes that its obligations under a collective bargaining
26 agreement would inhibit its effective reorganization, it must first
27 make a good faith effort to negotiate a modification of the
28 contract with its employees' authorized representative"); see also,
United Food and Commercial Workers Union, Local 328, AFL-CIO v.
Almac's Inc., 90 F.3d 1, 6 (1st Cir. 1996); Roth American, 975 F.2d
at 956, n.8.

1 This conclusion is inescapable in light of the fact that the
2 Stipulation was the result of lengthy negotiations involving not
3 only Debtor and Creditor, but Williams and the Creditors' Committee
4 as well. As the bankruptcy court in Equalnet (a case Creditor
5 cited) stated in dicta:

6 In a bankruptcy context, some issues clearly involve
7 interests upon which the parties such as the debtor, the
8 unsecured creditor's committee, the major lenders, and
9 major unsecured groups such as bondholders can agree. If
10 there is agreement among all of the constituencies and if
11 each of them is a sophisticated, competently represented,
12 knowledgeable constituency, the Court is generally loathe
13 to substitute its business judgment about the consequences
14 of the proposed course of action for that of the parties
15 that hold the real financial interest.

12 Equalnet, 258 B.R. at 370. All of the constituencies, each
13 represented by competent counsel, entered into negotiations in this
14 case regarding, inter alia, what was to be done with the CBA, and
15 the treatment to be given Creditor's pre-petition claim for health
16 benefits provided thereunder. The end result of those negotiations
17 was a Stipulation which specifically stated that the CBA "will not
18 be assumed at this time" and "permitted," but did not require, that
19 Debtor cure the pre-petition arrears. Williams' counsel testified
20 that the status to be accorded Creditor's claim was a key point in
21 these negotiations, and neither her client, nor the Creditors'
22 Committee would have agreed to any resolution which resulted in an
23 administrative claim.²⁶ Williams permitted Debtor to use his cash
24 collateral to continue its business on this basis. This Court will
25 not, under these circumstances, upset the agreement reached by the
26 parties in this case. To allow Creditor to obtain administrative
27

28 ²⁶ See Diemer Declaration, ¶ 5.

1 status for its claim under these circumstances would be both
2 inequitable and contrary to the clearly expressed intention of the
3 parties.

4 **B. Creditor's Necessity of Payment Argument**

5 The Court is likewise unswayed by Creditor's "necessity of
6 payment" argument. That doctrine is rooted in pre-Code decisions,
7 and is to be invoked only in extraordinary circumstances. In re
8 CoServ, LLC, 273 B.R. 487, 491-92 (Bankr. N.D. Tex. 2002). "[T]he
9 sine qua non for the application of the 'necessity of payment'
10 doctrine is the possibility that the creditor will employ an
11 immediate economic sanction, failing such payment." In re
12 Ionosphere Clubs, Inc., 98 B.R. 174, 176 (Bankr. S.D.N.Y. 1989).

13 This Court is not aware of any case where the necessity of
14 payment doctrine has been successfully invoked by a creditor where
15 there is a specific agreement that there will be no assumption, and
16 the creditor agreed to a specific treatment of its claim. Nor is
17 the Court aware of any case where, long after the theoretical
18 "necessity" had arisen, a creditor (rather than a Debtor) used the
19 doctrine to convert a pre-petition claim into an administrative
20 expense. Each of the cases Creditor cited -- none of which is
21 binding on this Court -- is, in any event, distinguishable. Two of
22 the cases each involved a chapter 11 debtor (rather than a
23 creditor) seeking to invoke the doctrine to authorize immediate
24 payment of pre-petition expenses it considered necessary to its
25 continued operations. Equalnet, 258 B.R. at 369; Gulf Air, 112
26 B.R. at 153. That is certainly not the case here, where Creditor
27 invoked the doctrine to gain administrative status for its claim,
28 and the Debtor opposed.

1 The Columbia Packing case Creditor cited, a bankruptcy court
2 case from the District of Massachusetts, is similarly unsupportive
3 of Creditor's position. It involved a debtor's apparently
4 uncontested request to pay pre-petition expenses, prior to plan
5 confirmation, in accordance with the priority scheme established by
6 § 507, which the court granted -- without even mentioning any
7 "necessity" of the payment. 35 B.R. at 448. Most importantly, the
8 case did not involve a negotiated agreement between the debtor and
9 its creditors, which is the exact situation here.

10 Likewise, the holding in Cajun Electric cannot be read to
11 support Creditor's argument that the necessity of payment doctrine
12 entitles its claim to administrative status in this case. In
13 assessing one of the settlements proposed in a trustee's plan of
14 reorganization, the trustee in Cajun Electric contended that the
15 necessity of payment doctrine would provide a valid defense to a
16 preference action. The objectors to the settlement and plan
17 countered the trustee's argument by asserting that the doctrine had
18 been limited to employee wage claims and certain other claims
19 otherwise entitled to priority under § 507. 230 B.R. at 754-755.
20 The bankruptcy court merely weighed the availability of preference
21 defenses as a factor in determining the reasonableness of the
22 proposed settlement. The context in which the court addressed the
23 necessity of payment doctrine -- evaluating proposed settlements --
24 is completely unlike the factual scenario in this case, where
25 Creditor attempted to invoke the doctrine to obtain administrative
26 status for its claim.

1 **C. Treatment of a Pre-petition Claim Where the CBA is Not Assumed**

2 We next turn to the manner in which Creditor's claim relating
3 to a pre-petition expense under an unassumed collective bargaining
4 agreement is to be treated. This Court finds the analysis in
5 Certified Air persuasive. In Certified Air, the bankruptcy court
6 followed decisions in the Second, Third and Fourth Circuits stating
7 that a claim arising from a default under an unassumed collective
8 bargaining agreement is not automatically treated as an
9 administrative claim. Certified Air, 300 B.R. at 369. Instead,
10 when the claim relates to a pre-petition period, it is treated
11 according to the priorities contained in § 507. Id.; see also,
12 Adventure Resources, 137 F.3d at 797; In re Ionosphere Clubs, Inc.,
13 22 F.3d 403, 408 (2d Cir. 1994); Roth American, 975 F.2d at 956.
14 Nothing in § 1113(f) or its legislative history indicates that
15 Congress intended for that section to override the priorities set
16 forth in § 507. Certified Air, 300 B.R. at 366-367.

17 Reconciliation of § 1113 with § 507 is preferable to an
18 interpretation that one section conflicts with or overrides the
19 other, and these sections should be interpreted to achieve equality
20 of distribution as a fundamental bankruptcy principle. Id. at 369.

21 Although Creditor relied on World Sales for its argument that
22 it had provided Debtor with a post-petition benefit akin to a
23 "loan" when it issued the credit to Debtor's employees, that case
24 is distinguishable. World Sales involved a claim for payments due
25 under an unrejected collective bargaining agreement for post-
26 petition work arising out of a post-petition breach of a collective
27 bargaining agreement. Due to the post-petition nature of the

1 claim, it was entitled to treatment as an administrative expense.
2 However, in this case, Creditor's claim is for pre-petition arrears
3 arising from a pre-petition breach of a collective bargaining
4 agreement that was not assumed. In addition, to the extent that
5 Creditor's post-petition loan argument is founded upon the idea
6 that Creditor granted the credit based upon Debtor's
7 representations that it would, in fact, cure the defaults, the
8 Stipulation provides otherwise and the Court is similarly
9 unconvinced. The language of the Letter -- which Creditor
10 repeatedly cites as evidence of Debtor's assurances²⁷ -- is
11 perfectly consistent with the language of the Stipulation -- that
12 Creditor would release the benefits upon payment of the
13 delinquency, and not before. This fact, coupled with the admission
14 of Creditor's counsel that the benefits were credited because of an
15 internal error, lead the Court to conclude that the credit was not,
16 in fact, given in reliance on Debtor's representation.²⁸

17 Creditor's unilateral mistake cannot transform the pre-petition
18 debt into an administrative claim. The Order permitting Debtor to
19 pay the arrearage over time was intentionally so structured to
20 avoid the creation of an administrative claim at the insistence of
21 Williams and the Creditors' Committee. Creditor's mistake in
22 crediting Debtor's employees with the benefits for the unpaid pre-
23 petition period cannot alter the effect of the Stipulation and
24

25 ²⁷ See Crowley Declaration, Ex. D.

26 ²⁸ Even if this were the case (despite the evidence to the
27 contrary), in the face of the language of the Stipulation, any such
28 reliance on Creditor's part was simply misplaced.

1 Order. Moreover, Debtor was completely unaware both that Creditor
2 was providing such benefits to Debtor's employees and that Creditor
3 had made this mistake.

4 The Court is not aware of any authority that would, under the
5 specific facts of this case, transform Creditor's claim for a pre-
6 petition expense under an unassumed collective bargaining agreement
7 from a priority claim into an administrative claim, whether or not,
8 as Creditor argues, that expense was "necessary" for preservation
9 of the estate. Accordingly, the Court declines to address whether,
10 and/or the extent to which, any benefit conferred on Debtor by
11 Creditor's mistaken credit of benefits for the unpaid pre-petition
12 period, of which Debtor was completely unaware, could constitute an
13 actual and necessary expense under § 503(b)(1)(A) in a different
14 factual setting (i.e., in the absence of the Stipulation and
15 Order).

16 The Court finds that Creditor's claim is not an administrative
17 claim but is instead a priority claim under §§ 507(a)(3) and (4).
18 Section 507(a)(4) specifies fourth priority for:

19 allowed unsecured claims for contributions to an employee
20 benefit plan--

21 (A) arising from services rendered within 180 days
22 before the date of the filing of the petition or the date
23 of the cessation of the debtor's business, whichever occurs
24 first; but only

25 (B) for each such plan, to the extent of--

26 (i) the number of employees covered by each such
27 plan multiplied by \$4,925; less

28 (ii) the aggregate amount paid to such employees
under paragraph (3) of this subsection, plus the
aggregate amount paid by the estate on behalf of
such employees to any other employee benefit
plan.

1 11 U.S.C. § 507(a)(4). According to § 507(a)(4), the amount must
2 be reduced by the amount of claims under § 507(a)(3). Section
3 507(a)(3) provides third priority to allowed unsecured claims:

4 to the extent of \$4,925 for each individual or
5 corporation, as the case may be, earned within 90 days
6 before the date of the filing of the petition or the date
of the cessation of the debtor's business, whichever occurs
first, for-

7 (A) wages, salaries, or commissions, including
8 vacation, severance, and sick leave pay earned by an
individual; or

9 (B) sales commissions earned by an individual or by a
10 corporation with only 1 employee, acting as an independent
11 contractor in the sale of goods or services for the debtor
12 in the ordinary course of the debtor's business if, and
only if, during the 12 months preceding that date, at least
75 percent of the amount that the individual or corporation
earned by acting as an independent contractor in the sale
of goods or services was earned from the debtor.

13 11 U.S.C. § 507(a)(3).

14 The maximum limit of Creditor's employee benefit contribution
15 claim pursuant to § 507(a)(4) is \$128,050 -- calculated by
16 multiplying the number of participants (26) by \$4,925.00 (the
17 statutory claims' cap). This amount is then reduced by the amount
18 claimed by Creditor under § 507(a)(3), or \$30,427.10. Accordingly,
19 Creditor's claim under § 507(a)(3) is \$30,427.10, and its claim
20 under § 507(a)(4) is \$97,622.90 (\$128,050 - \$30,427.10). The
21 § 507(a)(4) claim is further reduced by payments made by Debtor
22 totaling \$69,798.60, yielding a final claim amount of \$27,824.30.
23 Thus, as the parties stipulated at the January 20, 2006 hearing,
24 the total amount of Creditor's claim is \$58,251.40. The Court
25 finds that Creditor has a priority claim as follows: \$30,427.10
26 under § 507(a)(3) and \$27,824.30 under § 507(a)(4), for a total
27 claim of \$58,251.40.

IV.

CONCLUSION

For the reasons stated above, Creditor's Allowance Motion is denied. Pursuant to the parties' stipulation, made on the record, Creditor is entitled to a priority claim under §§ 507(a)(3) and (4) in the amount of \$58,251.40.

Counsel for Debtor shall submit a form of order so providing, after review by Creditor as to form.

Dated: 10/11/06


ARTHUR S. WEISSBRODT
UNITED STATES BANKRUPTCY JUDGE

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